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RUCPDO/DEPT OF COMMERCE WASHINGTON DC PRIORITY
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SUBJECT: STATUS OF PAKISTAN'S ENERGY SECTOR DEBT HOLDING
COMPANY

REF: A. ISLAMABAD 2381
[1](#)B. ISLAMABAD 2140
[1](#)C. ISLAMABAD 1983
[1](#)D. 08 ISLAMABAD 1623

[1](#)1. (SBU) Summary: While the GOP has taken some concrete steps to return the Pakistani energy sector to financial solvency, several key elements remain unresolved. On October 1, the GOP raised tariff rates by 6 percent, the first of three tariff hikes agreed with international financial institutions (IFIs) to bring revenue collections in line with costs. Although the GOP has injected \$1 billion into the system to deal with more recent arrears and is servicing some \$2.6 billion in old debt, the GOP has not yet moved this debt from the power sector's books to a debt holding company, as it committed to do. Nor has the GOP agreed on the holding company's corporate structure; decided specifically how it will restructure the debt; or determined what type of assets, if any, it will hold. The October 23-24 Energy Dialogue will provide an opportunity for USG experts to weigh in on (among other issues) how best to structure the holding company and ultimately pay off the debt. End Summary.

Background

[1](#)2. (SBU) Inter-corporate or "circular debt" is the result of non-payment between the various levels of and players in the energy sector, consumers, nonpayment for power provided, and the GOP's failure to pay power producers on the difference between the cost of providing power and the price at which they are allowed to sell it.

[1](#)3. (SBU) To deal with some \$4 billion in circular debt and prevent future recurrence, the GOP has agreed to a multi-part, multi-stage plan with the international financial institutions (IFIs). The GOP has agreed to raise rates over the course of the coming Pakistani fiscal year (July 1, 2009-June 30, 2010) sufficiently to cover costs of production and distribution: 6 percent in October 2009, 12 percent on January 1, 2010 and 6 percent on April 1, 2010. They also agreed to create a holding company to which the debt would be moved, thus clearing the companies, books and freeing up their lines of credit.

Progress to Date: the Good News

14. (SBU) As reported ref A, the GOP raised tariffs 6 percent on schedule on October 1, with almost none of the feared public outcry. MoF Joint Secretary for Budget Talib Baloch confirmed on October 15 that the GOP is making interest payments on the old debt, to the tune of \$140 million in the first quarter of Pakistani FY10, and that the GOP has increased the FY10 budget allocation for such payments from \$360 million to \$480 million, which the MoF estimates is sufficient to cover interest payments in FY10. (Comment: ADB and we concur, provided no new debt is accrued. End Comment.) He added, however, that the GOP only planned on budgeting for interest payments through FY12, at which point he believed the debt obligation would be liquidated.

The Less Good News: Consolidating and Transferring the Debt

15. (SBU) The GOP has yet to place the \$2.6 billion in old debt and the \$1 billion in TFCs on to the Government Power Holding Company's books, however, despite having created the company in June. The GOP named Fazeel Asif CEO of the holding company in October, but has yet to establish a board or name a CFO. The MoF has yet to come to an agreement with the banks on how to transfer the debt from the utilities' books to the holding company. MoF Director General for Debt, Masroor Qureshi, blamed the transfer's delay on the MoF which

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he said lacked the capacity to effectively negotiate with the banks.

The Right Men for the Job?

16. (SBU) According to a resume he provided, Asif does not have a finance or energy sector background, except for some public relations consulting work with the Ministry of Water and Power. He holds an MBA from Nichols University in Boston and was Managing Director of World Call, a communications, cable and real estate firm from 2000 to 2004. In a meeting with Econoff, he admitted that he knew little about how the new holding company would function and was uncertain how much debt it would assume. Secretary Water and Power Shahid Rafi said he (Rafi) would chair the corporate board, with other board members coming from the Ministries of Finance and Water and Power. The board would "most likely" have five members, and possibly private sector representation. Asif said the private sector member would come from PEPCO, the government holding company for energy utilities, while Rafi said the member would come from the banks. Once decided, the composition of the board would be forwarded to Pakistan's Cabinet for approval. Both Asif and Rafi said the Government Power Holding Company would maintain a small staff of roughly 10 employees.

Competing Plans for Managing the Debt

17. (SBU) Asif said the holding company's liabilities would be offset by the transfer of unused power sector and GOP land assets. He said the holding company would develop commercial and residential projects that would "increase the assets' values five-fold." MoF Joint Secretary External Finance Saleem Sethi and Joint Secretary Budget Baloch said that a proposal to transfer the public distribution companies (DISCOS) from PEPCO to the holding company was being sent to Prime Minister Gilani for consideration. They added that the debt would be paid down from the proceeds of privatizing the DISCOS. Secretary Water and Power Rafi, however, said that no assets would be transferred to the holding company.

18. (SBU) There is also no agreement on how to structure the

debt itself. Some of our interlocutors said that the first step was to come to terms with the banks to move the debts to the holding company, while restructuring the debt to lengthen the terms and lower interest payments. Though they were unsure how to do so, they envisioned that the debt would eventually be broken up into term finance certificates (TFCs) or collateralized debt obligations (CDOs) and sold to mutual funds and other investors.

¶9. (SBU) DG Debt Qureshi, however, presented a competing vision, asserting that the GOP would be better off selling T-bills to pay off the debt. Currently, the GOP is paying roughly 15 percent interest on the debt; financed through T-bills, the interest would be under 13 percent. Qureshi admitted that this would push the GOP well over its IMF fiscal deficit requirements, but argued that under the current arrangement, the GOP was simply pursuing an expensive option to hide its debt obligations in the holding company.

¶10. (SBU) Comment: Although we have been repeatedly assured that resolution of the circular debt is "just around the corner," with "only a few details remaining to be worked out," it is clear that the GOP missed Finance Minister Tarin's August 31 deadline to resolve this issue (ref C). The selection of a relative neophyte to lead the holding company is potentially troubling, although we could be pleasantly surprised. We are more concerned with the decision to grant the chairmanship of the holding company to the Ministry of Water and Power rather than Finance, and the lack of an agreed plan for the holding company, despite it

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having been established for several months. The delay notwithstanding, ADB has counseled patience, noting that the financial transfer requires a series of complex negotiations.

End comment.
PATTERSON